

CHRISTI CRADDICK, *CHAIRMAN*
RYAN SITTON, *COMMISSIONER*
WAYNE CHRISTIAN, *COMMISSIONER*



DANA AVANT LEWIS, *DIRECTOR*

RAILROAD COMMISSION OF TEXAS

HEARINGS DIVISION

OIL & GAS DOCKET NO. 03-0316365

Application of Gaither Petroleum Corporation (292850) Pursuant to Statewide Rule 78 for Reduction of Financial Security for the Beaumont Petroleum Co. – State (01771) Lease and the Stateland Oil Company (01777) Lease, Goose Creek Field, Harris County, Texas

PROPOSAL FOR DECISION

EXAMINERS:

Jennifer Cook
Administrative Law Judge
Ashley Correll, P.G.
Technical Examiner

PROCEDURAL HISTORY:

Hearing Date - January 29, 2019
Transcript Received and Close of Record - March 1, 2019
Proposal for Decision Issued - April 30, 2019

APPEARANCES:

For Applicant Gaither Petroleum Corporation -

Kelli Kenney, Attorney
McElroy, Sullivan, Miller & Weber

For Railroad Commission Staff -

Melissa Glaze, Staff Attorney
Office of General Counsel, Enforcement Section

For Observer Standton Capital -

Ryan Lammert, Attorney
McGinnis Lochridge

Table of Contents

I.	Statement of the Case.....	3
II.	Jurisdiction and Notice	3
III.	Applicable Legal Authority	4
IV.	Discussion of Evidence	7
	A. Summary of Applicant’s Evidence and Argument.....	7
	B. Summary of Staff’s Evidence and Argument	10
V.	Examiners’ Analysis	11
VI.	Recommendation, Proposed Findings of Fact and Proposed Conclusions of Law.....	12

I. Statement of the Case

Gaither Petroleum Corporation (“Applicant” or “Gaither”), Operator No. 292850, filed an application (“Application”), pursuant to Statewide Rule 78,¹ requesting a reduction in the amount of financial security to be filed with the Railroad Commission (“Commission” or “RRC”) concerning its Beaumont Petroleum Co. – State Lease, Lease No. 01771, and its Stateland Oil Company Lease, Lease No. 01777, (collectively referred to as “Leases”), both in the Goose Creek Field in Harris County, Texas. Commission staff (“Staff”) participated in this proceeding and opposes the Application. Standton Capital attended the hearing for this case as an observer only.

Applicant contends its financial assurance requirement for the bay wells on the Leases should be reduced based on plugging estimates it obtained from affiliate businesses. Applicant’s estimates do not include all plugging costs due to equipment and other costs Applicant would bear if it were to accept the bids. Applicant acknowledged the purpose of financial assurance is to provide funds for the Commission to pay plugging costs in the event that Applicant does not and defaults on its plugging obligations.

Staff contends Applicant should not be given a reduction in financial assurance and should be required to provide the financial assurance required in Statewide Rule 78, which is \$60,000 per bay well. Staff provided evidence that the lowest yearly average plugging cost that the Commission paid over fiscal years 2001-2018 was over \$60,000.

The Administrative Law Judge and Technical Examiner (collectively “Examiners”) respectfully submit this Proposal for Decision (“PFD”) and recommend the Commission deny Applicant’s request. The Examiners recommend the Commission find Applicant did not provide clear and convincing evidence that Applicant should get a reduction in financial assurance for the bay wells on the Leases.

II. Jurisdiction and Notice²

Sections 81.051 and 81.052 of the Texas Natural Resources Code provide the Commission with jurisdiction over all persons owning or engaged in drilling or operating oil or gas wells in Texas, and the authority to adopt all necessary rules for governing and regulating persons and their operations under the jurisdiction of the Commission.

On December 18, 2018, the Hearings Division of the Commission sent a Notice of Hearing (“Notice”) to Applicant, setting a hearing date of January 29, 2019. Consequently, Applicant received more than 10 days’ notice. The Notice contains (1) a statement of the time, place, and nature of the hearing; (2) a statement of the legal authority and jurisdiction under which the hearing is to be held; (3) a reference to the particular sections of the statutes and rules involved; and (4) a short and plain statement of the matters

¹ 16 Tex. Admin. Code § 3.78.

² The hearing transcript in this case is referred to as “Tr. at [pages].” Applicant’s exhibits are referred to as “Applicant Ex. [exhibit no(s)].” Staff’s exhibits are referred to as “Staff Ex. [exhibit no(s)].”

asserted.³ The hearing was held on January 29, 2019, as noticed. Applicant and Staff appeared and participated at the hearing.

III. Applicable Legal Authority

Applicant requests a reduction in financial security required to be filed for bay wells on the Leases. The definitions for financial security and bay wells are:

(4) Financial security--An individual performance bond, blanket performance bond, letter of credit, or cash deposit filed with the Commission.⁴

(5) Bay well--Any well under the jurisdiction of the Commission for which the surface location is either:

(A) located in or on a lake, river, stream, canal, estuary, bayou, or other inland navigable waters of the state and which requires plugging by means other than conventional land-based methods, including, but not limited to, use of a barge, use of a boat, dredging, or building a causeway or other access road to bring in the necessary equipment to plug the well; or,

(B) located on state lands seaward of the mean high tide line of the Gulf of Mexico in water of a depth at mean high tide of not more than 100 feet that is sheltered from the direct action of the open seas of the Gulf of Mexico.⁵

Commission rules require operators of wells in Texas to file financial security in one of the following forms:

(1) an individual performance bond;

(2) a blanket performance bond; or

(3) a letter of credit or cash deposit in the same amount as required for an individual performance bond or blanket performance bond.⁶

Statewide Rule 78(g)(1) requires the following regarding the amount of financial security operators have to file for wells:

(1) Types and amounts of financial security required.

³ See Tex. Gov't Code §§ 2001.051, 052; 16 Tex. Admin. Code §§ 1.42, 1.45.

⁴ 16 Tex. Admin. Code § 3.78(a)(4).

⁵ 16 Tex. Admin. Code § 3.78(a)(5).

⁶ 16 Tex. Admin. Code § 3.78(d).

(A) A person operating one or more wells may file an individual performance bond, letter of credit, or cash deposit in an amount equal to the sum of \$2.00 for each foot of total well depth for each well operated, excluding any well bore included in a well-specific plugging insurance policy.

(B) A person operating one or more wells may file a blanket bond, letter of credit, or cash deposit to cover all wells for which a bond, letter of credit, or cash deposit is required in an amount equal to the sum of the base amount determined by the total number of wells operated excluding any well bores and/or permits issued to drill, recompleat, or reenter wells included in a well-specific plugging insurance policy. A person performing multiple operations shall be required to file only one blanket bond, letter of credit, or cash deposit unless the person is operating a commercial facility, in which case the person also shall comply with the financial security requirements of subsection (I) of this section. The financial security amount shall be at least the base amount determined by the total number of wells operated or \$25,000, whichever is greater. After excluding any well bores and/or permits issued to drill, recompleat or reenter wells included in a well-specific plugging insurance policy, the base amount is determined as follows:

- (i) The base amount for a person operating 10 or fewer wells or performs other operations shall be \$25,000.
- (ii) The base amount for a person operating more than 10 but fewer than 100 wells shall be \$50,000.
- (iii) The base amount for a person operating 100 or more wells shall be \$250,000.⁷

Operators of bay wells have to file financial security in addition to the amount required in Statewide Rule 78(g)(1) as follows:

(3) Additional financial security for bay wells.

(A) All operators of bay wells shall file additional financial security of no less than \$60,000 in addition to any other financial security that is required under this section for any other Commission-regulated activities.

(B) For each bay well that is not currently producing oil or gas and has not produced oil or gas within the past 12 months, including injection and disposal wells, the operator shall file additional financial security of \$60,000, unless the well bore is included in a well-specific

⁷ 16 Tex. Admin. Code § 3.78(g)(1).

plugging insurance policy that provides benefits of at least \$60,000. An operator shall not be required to file additional financial security in addition to the \$60,000 amount set under subparagraph (A) of this paragraph if the operator operates only a single inactive bay well.

(C) In the case of a bay well that has been inactive for 12 consecutive months or longer and that is not used for disposal or injection, the well shall remain subject to the provisions of subparagraph (B) of this paragraph, regardless of any minimal activity, until the well has reported production of at least 10 barrels of oil for oil wells or 100 mcf of gas for gas wells each month for at least three consecutive months.⁸

Commission rules do allow operators of inactive bay wells to request a reduction in the financial security requirement as follows:

(5) Reduction in additional financial security required for bay and/or offshore wells that are not actively producing oil and natural gas. An operator may request that Commission consider a reduction in any additional financial security requirement for the operation of bay and/or offshore wells that are not actively producing oil and natural gas or that are used for disposal or injection in an amount not to exceed the remainder of 25% of the operator's certified net worth based on the independently audited calculation for the most recently completed fiscal year minus the Commission's estimate of the operator's total plugging liability for all of the operator's active bay and/or offshore wells.

(A) The director may administratively grant a full or partial reduction if the operator meets the following criteria:

(i) the operator has either five or fewer bay and offshore wells or at least half of the operator's bay and offshore wells are actively producing oil and natural gas;

(ii) the operator provides to the Commission certification of its net worth from an independent auditor that has employed generally accepted accounting principles to confirm the operator's stated net worth based on the most recently available and independently audited calculation;

(iii) the reduction is less than or equal to the remainder of 25% of the operator's certified net worth minus the Commission's estimate of the operator's total plugging liability for all of the operator's active bay and offshore wells;

⁸ 16 Tex. Admin. Code § 3.78(g)(1), (g)(2)

(iv) none of the operator's wells or operations, including any land-based wells, have been found by Commission staff to be violating or to have violated any Commission rule that resulted in pollution or in any hazard to the health or safety of the public in the last 12 months.

(B) If the director administratively denies the requested reduction, an operator may request a hearing to determine if a full or partial reduction should be granted.

(C) The operator may also request a hearing to challenge the Commission's presumed estimate of the operator's plugging liability for bay and offshore wells as applied to any additional financial security required for any inactive bay and offshore wells. The operator shall present clear and convincing evidence that the estimated plugging liability is less than the amount estimated by the Commission. Notice of the hearing shall be provided by the Commission to the owners of the surface estate and the owners of the mineral estate for any well that is a subject of the requested hearing, and all other affected persons as identified by the operator or otherwise required by the Commission.⁹

In this case, Applicant seeks a reduction in the estimated plugging liability for the subject wells, which is \$60,000 per bay well.¹⁰ Per Statewide Rule 78, Applicant is required to “present clear and convincing evidence that the estimated plugging liability is less than the amount estimated by the Commission.”¹¹

IV. Discussion of Evidence

Applicant provided one witness and 22 exhibits. Staff provided one witness and five exhibits.

A. Summary of Applicant’s Evidence and Argument

Applicant’s only witness was Mr. Orville Duane Gaither, II, Applicant’s President and CEO. He is a petroleum engineer and provided expert testimony. Gaither operated the subject wells in the past, and its current goal is to have the subject wells transferred to Gaither as the Commission operator of record.¹²

The subject wells are located in upper Galveston Bay in the Tabbs Bay area. The subject wells are in the Goose Creek Field. Applicant seeks a reduction in financial security for two leases, the Beaumont Petroleum Co. – State Lease (“BPC Lease”), Lease No. 01771, and its Stateland Oil Company Lease (“Stateland Lease”), Lease No. 01777.

⁹ 16 Tex. Admin. Code § 3.78(g)(5).

¹⁰ 16 Tex. Admin. Code § 3.78(g)(2)(B).

¹¹ 16 Tex. Admin. Code § 3.78(g)(5)(C).

¹² Tr. at 19-21.

The current operator of record for the Leases is Siempre Energy Operating, LLC (“Siempre”). There are 20 wells on the BPC Lease. All are either shut in or not producing. There are nine wells on the Stateland Lease. All are either shut in or not producing. None of the wells on the Leases are on the Commission’s orphan well list.¹³

Applicant provided documentation that the underlying contractual leases between Siempre and the Texas General Land Office (“GLO”) have terminated due to lack of production. Applicant would like to take over the Leases and bring them back into production. Consequently, Applicant entered into contractual leases (“Contractual Leases”) with the GLO covering the Leases.¹⁴

After executing the Contractual Leases, Applicant filed with the Commission Form P-4s *Certificate of Compliance and Transportation Authority* (“Form P-4s”), one for each of the Leases, requesting that it be designated the Commission operator of record for the Leases. Initially, Applicant filed them without the signature of the current operator, Siempre. Ultimately, Applicant was able to obtain Siempre’s signatures on the Form P-4s for both Leases. The Form P-4s can not be approved until financial assurance is established. Gaither obtained contractual leases covering 16 land wells near the Leases that were previously operated by Siempre and were non-productive; Gaither has successfully transferred those wells via Form P-4s and returned 14 of 16 wells back into production.¹⁵

Gaither is an active operator registered with the Commission. Gaither currently has a bond in the amount of \$250,000 as its financial security on file with the Commission. Mr. Gaither testified that Applicant has been a bonded operator with the Commission since 1992.¹⁶

Mr. Gaither testified the Stateland Lease has not been maintained by Siempre and is in disrepair. According to Mr. Gaither and letters issued by Staff, there have been spills and leaks on the Stateland Lease. In letters issued by Staff, Staff notifies Siempre that the Stateland Lease is not in compliance with Statewide Rule 8, threatens to pollute or is polluting surface or subsurface water, and contains abandoned wells that are leaking or likely to leak. Staff directs Siempre to clean up the Leases and plug the wells, and states if Siempre does not, the Commission may do so with state funds and thereafter seek reimbursement. Mr. Gaither testified that Applicant has provided a temporary fix on a leaking flow pipe with a boom and clamp. An epoxy patch has been placed on a leaking tank battery. Mr. Gaither asserts these are temporary fixes that may not hold so there is still a threat of pollution. He claims if Applicant can get this lease transferred from Siempre to Applicant via the Form P-4s, Applicant is ready and has the necessary equipment to bring the Stateland Lease into compliance with Commission rules.¹⁷

¹³ Tr. at 22-29; Applicant Ex. 1-6.

¹⁴ Tr. at 29-33; Applicant Ex. 7-10.

¹⁵ Tr. at 34-39; Applicant Ex. 11-13.

¹⁶ Tr. at 39-40; Applicant Ex. 14.

¹⁷ Tr. at 41-49; Applicant Ex. 15-17.

Mr. Gaither testified that he believes the wells on the Leases have potential and should not be put on the Commission's orphan well list. He has performed an analysis of remaining reserves and believes there are significant reserves that can still be produced, and Gaither is interested in producing them.¹⁸

Mr. Gaither provided an estimate for plugging the wells. The estimates are based on bids from businesses affiliated with Applicant, including Innovative Energy Services, Inc. ("Innovative Energy") and Wireline & Perforating Company. Mr. Gaither's estimate includes a \$24,962.35 credit due to salvage. His total estimate, subtracting the credit amount, is \$700,873.51. He testified that there is a 10 percent discount if the operator pays within 10 days. With this discount, his estimated total cost is \$630,786. Mr. Gaither provided 29 invoices from Innovative Energy, one for each of the wells on the Leases.¹⁹ During testimony, Mr. Gaither referred to the affiliated businesses as "we." For example, he testified:

THE WITNESS: We have to -- Innovative has to file the W-3s within 30 days of abandonment. And some operators have a tendency to drag their feet on payment. Not saying the Railroad Commission is one. But some operators do. So we offer a 10 percent discount to people that pay within ten days.

QUESTION: Who is "we"?

THE WITNESS: The Innovative Energy Services . . . provides a 10 percent discount to operators that pay within ten days so that we can get the P-4 -- the W3 in to the Railroad Commission timely.²⁰

He testified that the estimate does not include an estimate for the barge and tug that would be required because Gaither owns the tug.²¹ Innovative Energy is an active operator on file with the Commission and an approved cementer for plugging wells. It has a bond in the amount of \$25,000 on file with the Commission as financial security.²²

Mr. Gaither requests that Applicant's financial security for the Leases' bay wells be \$700,873.51 instead of \$60,000 per bay well for a total of \$1,740,000, as required by Statewide Rule 78. This financial security for the Leases' bay wells would be in addition to the \$250,000 base financial assurance it currently has on file. He testified that this is also in addition to a \$60,000 fee, that he refers to as an "entry fee" to operate bay wells, also required in Statewide Rule 78.²³ He testified:

¹⁸ Tr. at 49-54; Applicant Ex. 18.

¹⁹ Tr. at 54- 64; Applicant Ex. 19, 20.

²⁰ Tr. at 56:25 to 57:14.

²¹ Tr. at 61-62.

²² Tr. at 64-66.

²³ Tr. at 66-69; Applicant Ex. 22.

I'm asking that the Railroad Commission consider the capabilities of Gaither Petroleum and its affiliates.²⁴

B. Summary of Staff's Evidence and Argument

Staff's only witness was Mysti Doshier. She is the manager of the P-5/Financial Assurance Unit. According to Commission Form P-5 records, Gaither operates 320 wells, 146 of which are inactive and all of which are land wells.²⁵

According to Commission Form P-5 records, Siempre is the Commission record operator of 35 wells, all of which are inactive bay wells; Applicant wants to have 29 of them transferred to it. Ms. Doshier testified Siempre would need to file \$2,040,000 in financial assurance to renew its Form P-5 and achieve active status again with the Commission. According to her testimony, the Commission has never reduced Siempre's financial assurance obligation.²⁶

Ms. Doshier provided the Commission's Oil and Gas Division's Field Operations' state-managed average plugging cost per foot for fiscal years 2001 through 2018. The annual average cost of plugging bay wells during this timeframe is between \$60,103 and \$512,944. The annual average cost per foot of depth is between \$8.22 and \$276.07. These amounts are based on Field Operations' actual costs paid for plugging wells. These averages are used to predict costs.²⁷ She testified that the wide range of costs reflects the variety of issues that can arise when plugging a bay well and that are only discovered after plugging of the well commences.²⁸

Ms. Doshier explained that one option for Applicant is to transfer one of the Leases, bring it back into production and then get a reduction of the financial assurance once the wells are back in production.²⁹ She testified:

THE WITNESS: An operator could come in and take with the amount of financial assurance that they're able to come up with, they would be able to come in and take a one lease, get that well up and running, get the well producing by Commission definition, which would lower their financial security amount, which would allow them to take over additional leases at a slower pace. Right? It wouldn't be everything all at once, but there would be a mechanism for them to be able to do that.

²⁴ Tr. at 68:5 to 68:7.

²⁵ Tr. at 71-74; Staff Ex. 1-2; Mr. Gaither testified that Gaither had sold its interests in between 135-140 wells. However, that is not equivalent to the wells being transferred from Gaither as the Commission operator of record. Gaither provided no documentation that Gaither has transferred any of its wells to another operator as Commission operator of record. Tr. at 99-100.

²⁶ Tr. at 74-80, 88-89; Staff Ex. 3-4.

²⁷ Tr. at 80-86; Staff Ex. 5.

²⁸ Tr. at 91-93.

²⁹ Tr at 86-88.

QUESTION: So once it's produced then that extra amount would either go away or be reduced?

THE WITNESS: Well, it would be able to be reduced. We would be able to look at that. Typically, it's done at a renewal time. So each renewal cycle is when we normally would look at that. But in the event of a situation like this, we would take those things into account, and we would work through that process with the operator. I mean, it would be obviously in everybody's best interest for the operator to take these wells over. However, you know, we have statutory limits and obligations related to financial security requirements.³⁰

In rebuttal, Mr. Gaither testified that Applicant prefers not to transfer one of the Leases and get the wells into production in order to get reduced financial assurance as discussed by Ms. Doshier. Mr. Gaither believes some of the wells could be returned to production easily, so Applicant does not want to go slowly.³¹

Mr. Gaither further testified that his plugging bids are lower than what Staff pays because his bids do not contain costs associated with hiring the tug and the barge, the rig, the crew, the perforator or the wireline to set the bridge plugs, because Applicant owns those already. The bids are for labor, diesel fuel and insurance.

Mr. Gaither acknowledged the financial assurance would only be implicated if Gaither defaults and fails to pay plugging costs for wells for which it is the operator of record. Financial assurance comes into play when the Commission needs to get a bid and pay the cost of plugging a well. He acknowledged the Commission would not be able to obtain a bid similar to the bids obtained by Gaither from its affiliate business. There are costs that are not included in Gaither's affiliates' bids because of some equipment that is already owned by Gaither.³² Mr. Gaither did state, "I'm sure we would lend them to you."³³

Staff opposes Applicant's request for a reduction of financial assurance and is requesting that Gaither be required to file the amount of financial assurance required by Commission rules. Statewide Rule 78 requires \$60,000 in financial assurance to become an operator of bay wells and then an additional \$60,000 for each well.³⁴

V. Examiners' Analysis

The Examiners recommend Applicant's request for relief be denied. The Examiners recommend the Commission find Applicant failed to provide clear and

³⁰ Tr. at 87:13 to 88:10.

³¹ Tr. at 100-102.

³² Tr. at 107-108.

³³ Tr. at 107:24.

³⁴ See, e.g., Tr. at 93, 109.

convincing evidence that Applicant should get a reduction in financial assurance for the bay wells on the Leases.

As Applicant acknowledged, financial assurance is used by the Commission when the Commission has to pay plugging costs because an operator does not pay its plugging obligations. Applicant provided bids from affiliate businesses. Applicant provided insufficient evidence the bids are the equivalent of an arms-length transaction reflecting actual market costs. Applicant's bids did not contain all costs associated with plugging. For example, Applicant's bids did not contain costs regarding equipment Applicant has and would not have needed. Applicant provided bids which are estimates and do not reflect actual amounts paid.

Staff provided documentation of actual amounts paid by the Commission over an 18-year timeframe for plugging bay wells. The lowest annual average cost of plugging a bay well was more than the \$60,000 amount required as financial assurance in Statewide Rule 78. Applicant provided insufficient evidence that the Commission would be able to plug the bay wells on the Leases for the amount in Applicant's bids.

For these reasons, the Examiners recommend the Commission find Applicant failed to provide clear and convincing evidence Applicant should get a reduction in financial assurance for the bay wells on the Leases and deny Applicant's request for relief.

VI. Recommendation, Proposed Findings of Fact and Proposed Conclusions of Law

Based on the record and evidence presented, the Examiners recommend the Commission find Applicant failed to provide clear and convincing evidence that Applicant should get a reduction in financial assurance for the bay wells on the Leases, deny Applicant's request for a reduction in financial security, and adopt the following findings of fact and conclusions of law.

Findings of Fact

1. Gaither Petroleum Corporation ("Applicant" or "Gaither"), Operator No. 292850, filed an application ("Application"), pursuant to Statewide Rule 78,³⁵ requesting a reduction in the amount of financial security to be filed with the Railroad Commission ("Commission" or "RRC") concerning its Beaumont Petroleum Co. – State Lease, Lease No. 01771, and its Stateland Oil Company Lease, Lease No. 01777, (collectively referred to as "Leases"), both in the Goose Creek Field in Harris County, Texas. Commission staff ("Staff") participated in this proceeding and opposes the Application. Standton Capital attended the hearing for this case as an observer only.
2. Applicant is not the Commission operator of record for the Leases. Applicant seeks a reduction in the amount of financial assurance required for the wells on the

³⁵ 16 Tex. Admin. Code § 3.78.

Leases in an effort to get the wells transferred to Applicant as the Commission operator of record.

3. The subject wells on the Leases are 29 bay wells in Harris County.
4. On December 18, 2018, the Hearings Division of the Commission sent a Notice of Hearing (“Notice”) to Applicant, setting a hearing date of January 29, 2019. Consequently, Applicant received more than 10 days’ notice. The Notice contains (1) a statement of the time, place, and nature of the hearing; (2) a statement of the legal authority and jurisdiction under which the hearing is to be held; (3) a reference to the particular sections of the statutes and rules involved; and (4) a short and plain statement of the matters asserted.³⁶ The hearing was held on January 29, 2019, as noticed. Applicant and Staff appeared and participated at the hearing.
5. The Commission tracks the Commission’s Oil and Gas Division Field Operations’ state-managed average plugging cost per foot for fiscal years 2001 through 2018. The annual average cost of plugging bay wells during this timeframe is between \$60,103 and \$512,944. The annual average cost per foot of depth is between \$8.22 and \$276.07. These amounts are based on Field Operations’ actual costs paid for plugging wells.
6. The actual cost of plugging a bay well can be unpredictable due to the variety of issues that can arise when plugging a bay well and that are only discovered after plugging of the well commences.
7. The Commission’s estimated cost for plugging a bay well is \$60,000 pursuant to Statewide Rule 78.
8. The lowest annual average cost of the Commission for plugging a bay well was more than the \$60,000 amount required as financial assurance in Statewide Rule 78.
9. Applicant provided bids totaling \$700,873.51 to plug the 29 bay wells on the Leases.
 - a. The bids are from affiliate businesses of Applicant. It is not clear the amounts reflect market costs based on arms-length transactions.
 - b. Applicant’s bids do not contain costs associated with hiring the tug and the barge, the rig, the crew, the perforator or the wireline to set the bridge plugs, because Applicant owns those already. The bids are for labor, diesel fuel and insurance. Consequently, Applicant’s bids do not contain amounts for all the costs that would be incurred for plugging a bay well.
 - c. Applicant provided bids which are not actual amounts paid.

³⁶ See Tex. Gov’t Code §§ 2001.051, 052; 16 Tex. Admin. Code §§ 1.42, 1.45.

10. Financial assurance is used by the Commission when the Commission has to pay plugging costs because an operator does not pay its plugging obligations.
11. Applicant provided insufficient evidence that the Commission would be able to plug the bay wells on the Leases for the amount in Applicant's bids.

Conclusions of Law

1. Proper notice of hearing was timely issued to persons entitled to notice. *See, e.g.*, Tex. Gov't Code §§ 2001.051, 052; 16 Tex. Admin. Code §§ 1.42, 1.45, 3.78.
2. The Commission has jurisdiction in this case. *See, e.g.*, Tex. Nat. Res. Code § 81.051.
3. Applicant failed to provide clear and convincing evidence that the estimated plugging liability for the 29 bay wells on the Leases is less than the amount estimated by the Commission, which is \$60,000 pursuant to Statewide Rule 78. 16 Tex. Admin. Code § 3.78.
4. Applicant's request for a reduction in financial security based on Applicant's estimates should be denied.

Recommendations

The Examiners recommend the Commission find Applicant failed to provide clear and convincing evidence that Applicant should get a reduction in financial assurance for the bay wells on the Leases and deny Applicant's request for a reduction in financial security.

Respectfully,



Jennifer Cook
Administrative Law Judge



Ashley Correll, P.G.
Technical Examiner